

### Inclusive growth: the case of Germany

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Schmid, Günther

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POLICY PAPER SERIES

IZA Policy Paper No. 139

**Inclusive Growth: The Case of Germany**

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JUNE 2018

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### **Inclusive Growth: The Case of Germany**

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JUNE 2018

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## ABSTRACT

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### **Inclusive Growth: The Case of Germany<sup>1</sup>**

This paper argues that inclusive growth appears to be the only suitable strategy for realising the right to decent work (RDW) in the digital economy. This reasoning is in blunt opposition to the current mood of giving up this right in favour of an unconditional basic income (UBI). The study starts by briefly expanding the basic argument and by defining the principles of inclusive versus exclusive growth (1); a comprehensive overview of German labour market policy and labour law reforms since the beginning of this millennium assesses to what extent Germany is pursuing these principles, accompanied by selective evidence of their consequences for the German labour market performance (2); a stylised and descriptive overview of the inclusive impact of these reforms in quantitative and qualitative terms follows, with an essay reflecting the concept of the inclusive labour contract (3).

**JEL Classification:** J41, J48, K31, K38, O43, R11

**Keywords:** labour market policy, labour law, human right law, inclusion, institutions, growth, non-standard work, Germany

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## Introduction

The argument I would like to bring forward is that inclusive growth appears to be the only suitable strategy for realising the right to decent work (RDW) in the digital economy. This reasoning is in blunt opposition to the current mood of giving up this right in favour of an unconditional basic income (UBI). The RDW has three advantages over UBI: First, the RDW corresponds to the most important and universally accepted principles of ethics, whereas UBI has some important flaws in this respect; second, the RDW is a realistic and evolutionary reform perspective, whereas UBI is an unrealistic and disruptive utopia; and third, the RDW, through inclusive growth, promises to combine equity with efficiency whereas UBI endangers both.

In the following, I will (1) briefly expand the basic argument in general terms and define the basic principles of inclusive versus exclusive growth; (2) a comprehensive overview of German labour market policy and labour law reforms since the beginning of this millennium assesses to what extent Germany is pursuing these principles, accompanied by selective evidence of their consequences for the German labour market performance; (3) a stylised and descriptive overview of the inclusive impact of these reforms in quantitative and qualitative terms follows, with an essay reflecting the concept of the inclusive labour contract.

### 1. A right to decent work or an unconditional basic income?

The current debate on the future of work is obsessed with two interlinked ideas: the digital revolution will definitely destroy 50 to 90 percent of jobs and the only solution for the increasing mass of jobless people is a universal basic income (UBI). Whereas there is no room here to show that the first – in fact very old – idea stands on shaky theoretical and empirical fundamentals,<sup>2</sup> the other – in fact equally old – idea has recently been carefully scrutinised by the OECD. The summary of these reflections must also suffice here before entering into the main argument: “But an unconditional payment to everyone at meaningful but fiscally realistic levels would require tax rises as well as reductions in existing benefits, and would often not be an effective tool for reducing income poverty. Some disadvantaged groups would lose out when existing benefits are replaced by a BI, illustrating the downsides of social protection without any form of targeting at all. Realistically [...] reforms towards more universal income support would need to

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<sup>2</sup> Among others, with many further references: Arntz et al. (2016); Eichhorst/Buhlmann (2015); Schmid (2018b, chapter 2).

be introduced in stages, requiring a parallel debate on how to finance a more equal sharing of the benefits of economic growth.”<sup>3</sup>

Furthermore, there are strong ethical arguments which underline that the capability to earn one’s own living is a basic fundament of human dignity. Many constitutions and conventions refer to this ethical principle so that the hint to article 23 of the Universal Declaration of Human Rights from Philadelphia (1944/1948) should be enough: “Everyone has the right to work, to free choice of employment, to just and favourable conditions of work and to protection against unemployment.” The “ILO Declaration on Social Justice for a Fair Globalization” on 10 June 2008 reminds us again of this basic human right and again “affirms that labour is not a commodity”. This normative argument is backed by empirical research which consistently finds a strong connection of happiness with having a job: “If society’s goal is to increase people’s feelings of well-being, economic growth in itself will not do the job. Full employment and a generous and comprehensive social safety net do increase happiness.”<sup>4</sup>

Another line of ethical thinking goes back to Aristotle’s Nicomachean ethic, which states that human beings develop their capabilities and identities in taking personal risks and putting their “skin in the game”, i.e. being accountable and responsible for what they are doing. The UBI would exclude many individuals from this challenge and relieve employers and politicians from their responsibility of managing the social risks related to this challenge. Again, this argument would need further elaboration, which is not within the scope of this essay.<sup>5</sup>

Only providing income security would eventually deny these intrinsic values of work and lead to the exclusion of an increasing number of people from labour market participation. We would be faced with a polarised world of work in those who fit to the labour market and those who mainly live on UBI and earn – if they wish – something in addition without being exposed to the challenges of personal risk-taking.

So, what is the alternative to this dystopia? The right to decent work (RDW) through inclusive growth, an element – albeit not yet well developed – of the European Employment Strategy, might be the proper solution. Table 1 summarises the basic elements of this strategy compared to the strategy of UBI through exclusive growth.

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<sup>3</sup> OECD (2017, from the abstract).

<sup>4</sup> From the abstract of Easterlin (2012/13).

<sup>5</sup> See the stimulating and provocative book by Taleb (2018); for risk-taking and social risk management see Schmid (2011, 2015a, 2018b).

Table 1: Principles of inclusive growth versus exclusive growth

Right dimension	Inclusive growth through	Exclusive growth through
Right to gainful work	Labour market security through > minimising unemployment > employment protection > working time flexibility over the life course, in particular > internal flexibility	Labour market flexibility through > maximising employment > hire and fire > external flexibility
Equal treatment and active securities	> minimum wages > making the market fit to workers > making workers fit to the market > rights to active securities	> market wages > only making workers fit to the market > only rights to passive securities
Labour market status	Labour market citizen through > voice and negotiated flexibility > early access to gainful work > loose but continuous ties to LM > cooperative learning environment	Civic citizen through > entry and exit options > late access to gainful work > strong or no ties to LM > competitive learning environment
Social protection	> Social insurance (ex ante redistribution), in particular > anticyclical U-benefits > means-tested income guarantee	> Unconditional basic income (UBI)

Source: G. Schmid, own presentation.

Since the table speaks for itself, only the main points shall be emphasised:

- Concerning the right to gainful work, the overall objective of inclusive growth would be labour market security and therefore not to maximise employment as such but to *minimise unemployment*, among others through the protected flexibility of employment relationships, the maintenance of jobs through internal flexibility and public job guarantees.
- Concerning equal treatment, a strong emphasis would be put on the strategy of *making the market fit to workers* in order to overcome the various restrictions of individual earning capacities over the life course, in particular due to unpaid social work obligations and disabilities, among others through the reasonable adjustment of workplaces.
- Concerning the labour market status, inclusive growth emphasises early access to gainful work and voice through *negotiated flexibility*, above all through co-determination in collective agreements at the firm, regional or branch level.



- Concerning social protection, inclusive growth would accentuate social insurance principles with strong elements of ex ante redistribution through shared contributions to health, pension and unemployment insurance; this would, among others, allow anticyclical ('breathing') unemployment benefits or short-time work allowances to stabilise effective demand in cyclical troughs; UBI would tend to procyclical reactions.

In the following, the differences between the two strategies will become clearer when we examine the various labour market policy and law reforms, here exercised for the case of Germany. –

## 2. German labour market policy and labour law reforms since 2000

The recent German labour market reforms are commonly subsumed under the so-called 'Hartz reforms' adopted in 2003 and 2004.<sup>6</sup> Despite their prominence or even bad reputation (*Hartz IV*), other – and some even more important – reforms have to be mentioned under the inclusive perspective. To bring some order into the reforms, I shall use the analytical framework of transitional labour markets (TLM) which distinguishes five main risks of exclusion (the reverse to inclusion) over the life course:<sup>7</sup> (1) School to work transitions with the risk of insufficient earnings capacities; (2) job-to-job transitions or transitions between standard and non-standard employment with the risk of precarious jobs and volatile or too low earnings; (3) transitions between employment and unemployment with the risk of downward careers or even being permanently excluded; (4) transitions between family work or own work and employment with the risk of restricted earnings capacities and career interruption; (5) transitions between employment and inactivity due to old age or disablement with the risk of reduced earnings or even total loss of any earnings capacities.

### 2.1 *School-to-work transitions*

With respect to school-to-work transitions, there has been no basic labour market reform. The main reason is that the German system of school-to-work transitions already widely corresponds to the principles of inclusive growth. The dual system in the form of apprenticeship or tertiary vocational training combines theoretical with practical education as well as learning with gainful work, which means that young people can earn some part of their living while still being trained and educated for full earnings capacities. Youth unemployment is one of the lowest in Europe.

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<sup>6</sup> Due to the fact that chancellor Schröder did not follow the proposals by the Hartz Commission in some important respects (see Jann/Schmid 2004; Schmid 2011; Schmid 2017b), I will talk of the 'Schröder reforms' in the following.

<sup>7</sup> For the concept and theory of TLM see Schmid/Gazier (2002), Schmid (2008, 2017, 2018b).

This does not mean, however, that this system is without flaws. Even many of those who are included suffer, for instance, through an increase in non-standard forms of employment<sup>8</sup> and from low apprenticeship allowances. The new grand coalition (CDU/CSU and SPD) plans therefore, among others, to establish a *right to return from part-time* (e.g. combined with training) *to full-time work* on the one hand, and to introduce a *minimum wage for apprentices* on the other hand. These measures shall also increase the falling motivation to take up an apprenticeship and to stop the trend of young people entering university even though they lack the cognitive capacities, therefore facing a high risk of failure. About one-third of beginners drop out after two years, in particular in science subjects like mathematics, physics, chemistry and ICT.

The flip side of the coin is that the successful inclusion for most young people into the labour market has negative repercussions for those who face disadvantages in terms of physical capacities (e.g. disabilities), ethnic background (e.g. deficits in language and communication abilities) or lack of endowments with basic cognitive skills (e.g. reading, mathematics). Many of these disadvantaged remain stuck in the complex transition system maintained by labour market policy measures. In 2015, 6 percent of youth finished school without a certificate, and 13.4 percent of youth aged 20 to 34 were without a vocational training certificate (in total, almost two million); for those with a migration background this percentage is 29.8 percent.<sup>9</sup> So, almost two million young adults are excluded from sustainable labour market careers. The positive side is that legal reforms in recent decades have opened the access to universities also to youth with certified vocational training; the negative side is that those people without an occupational degree will never have the right to enter the universities.

Many piecemeal reforms for assisting those people were implemented. Meanwhile, the current grand coalition government plans more, for instance, so-called *assisted apprenticeship* (under the responsibility of the Labour Ministry) or *supported apprenticeship* (under the responsibility of the German PES<sup>10</sup>) – both intending to help on both sides of the labour market: the firms (in particular small enterprises) and the students, sometimes even including the parents; also large *investments in the digital infrastructure* of vocational training schools (*Berufsschulen*) have been announced.

In terms of inclusive growth and its principle of early access to work, one basic reform is still outstanding: As two centrepieces of the apprenticeship system are eroding, i.e. the small and medium-sized enterprises as the learning location and highly specialised occupations as the learning goal, a strategic reorientation of

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<sup>8</sup> See Schmid (2015b) and Figure 1 below.

<sup>9</sup> Berufsbildungsbericht (2017), p. 10.

<sup>10</sup> PES=Public Employment Service; in Germany ‘Bundesagentur für Arbeit’.

dual systems of learning seems to be logical: First, early access to work has to be provided more and more on a school basis; and second, occupational profiles have to be widened to increase the adjustment capacities to the quickly changing digital world of work. Switzerland and Austria (probably also Denmark and the Netherlands) seem to be model countries in this respect. In Austria, already 26 percent of youth aged around 16 attend full-time vocational colleges with integrated practical experiences in firms (*Berufliche Höhere Schulen*) providing both a licence for exercising a broadly defined occupation as well as the right to enter university (*Matura*). In Switzerland, one-third of youth attend business colleges or universities of applied sciences (*Fachhochschulen*) that also require practical experiences from both the teachers and the students. Both countries have better records than Germany in integrating youth into the labour market at their acquired skill levels, and both countries also do better for disadvantaged youth by ensuring some kind of accredited education that is marketable.<sup>11</sup>

## 2.2 *Job-to-job transitions*

The dynamics of job-to-job transitions in the German labour market is low and has even declined in recent decades compared, for instance, to the ‘flexicurity’ country Denmark.<sup>12</sup> This happened despite German labour market reforms intending to promote flexibility and security in the employment relationships. The labour-turnover-rate declined after the economic expansion in 2000 and 2001 and during the implementation of the Schröder reforms (2002–2010) and has not reached the level of 7 or 8 percent per year since then.<sup>13</sup> These reforms promoted three types of non-standard employment: self-employment, temporary jobs (in particular through temp-agency work), and marginal jobs, which will be briefly explained in the following.

Before going into details of these reforms, however, the reader shall be reminded that one reason for the low labour turnover in Germany is internal flexibility, in particular through working-time flexibility either in the form of collective agreements or in the form of *short-time working*. Both measures were heavily used as adjustment measures in the crisis of 2008/09 and correspond, in broad terms at least, to the principles of inclusive growth. As they are based on established labour market instruments and are familiar to the scientific community, I abstain from further explanations and details.<sup>14</sup>

(1) The new *start-up subsidy* (in Germany also called the ‘*Ich-AG*’) has been supplementing the already existing bridging allowance (*Überbrückungsgeld*, since 1986), which capitalised unemployment benefit entitlements in order to support

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<sup>11</sup> See Schmid (2015a) for further references and details.

<sup>12</sup> See Madsen (2006).

<sup>13</sup> Giannelli et al. (2013, p. 6).

<sup>14</sup> Among others see Schmid (2015b) for further references.

the unemployed in setting up their own businesses.<sup>15</sup> Whereas the individual amount of bridging allowance was derived from the unemployment benefit plus a lump sum of €300 per month for social insurance and was paid for only six months, the *Ich-AG* subsidy was paid as a yearly decreasing lump sum for three years, provided the recipient's annual income did not exceed €25,000. The risk associated with self-employment was cushioned by the fact that eligibility for unemployment benefits persisted for a period as long as four years.

The take-up of the start-up subsidy was much higher than expected, and against certain initial reservations it did not replace the bridging allowance. In addition, from the perspective of employers, the possibility of buying the services of a self-employed instead of hiring a dependent employed person is always an attractive option, since dismissal protection does not apply to this category of workers. So, one has to be careful since a careless promotion of self-employment might induce and increase unprotected fake self-employment. Furthermore, bureaucratic thresholds for employment creation were loosened: all business start-ups had the option of hiring additional employees on the basis of fixed-term contracts for up to four years.

Regarding the security dimension, minimum income security was provided in the form of a monthly allowance of 600 Euro in the first year, 360 Euro in the second year, and 240 Euro in the third year. Concerning social security, it is important to note that in contrast to regular self-employment, social insurance was obligatory as long as the *Ich-AG* founders were in receipt of the corresponding allowance. Although at first sight the *Ich-AG* seemed to provide the founder with minimum income security for three years, from the second year on the allowance only sufficed to cover the cost of social security contributions.

Even though evaluation research has given credit to this component of the Schröder reforms, the *Ich-AG* scheme was abolished in 2006 and merged with the more efficient bridging allowance to create an overall Start-up Allowance (*Gründungszuschuss*) for the unemployed. Since then, the take-up of this measure remained at a level of around 140,000 up to the end of 2011 when – in the vein of overall budget cuts – the regulation was sharply tightened: most important was the change from a so-called ‘obligatory measure’ (*Pflichtmaßnahme*) to a discretionary measure (*Ermessensmaßnahme*). In Germany an ‘obligatory’ measure means *having the right to be promoted* to self-employment if certain conditions are fulfilled. At the end of the day this means that the worker can go to court to claim his or her right.<sup>16</sup> A ‘discretionary’ measure means that it remains up to the administrator to decide on the measure depending on the labour market

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<sup>15</sup> This measure, of course, also belongs to the section on transitions between employment and unemployment.

<sup>16</sup> The success of short-time work goes back, among others, to still being an ‘obligatory’ measure, i.e. a right for the workers. Even works councils are entitled to apply for short-time work at the PES.

or – more commonly – budgetary conditions. The new discretionary measure was further tightened by the requirement that potential beneficiaries are still entitled to at least 150 days of insurance-related unemployment benefits (ALG I); in other words, having already exhausted these days, the unemployed are no longer entitled; the long-term unemployed are thus excluded.

Currently, the two basic features of the new start-up measure for the unemployed are: in the first six-month phase, the unemployment benefits are topped up by 300 Euro monthly so as to ensure the social security contributions of the self-employed; during the following second phase of nine months (after a judgement of whether the start-up will likely be sustainable), the beneficiary only receives the monthly allowance of 300 Euro. The result of this reform was a sharp drop in the number of participants, down to 20,000 from 30,000. The PES now plans to revitalise the measure by doubling the targeted budget, not least due to quite positive evaluations of this measure.<sup>17</sup>

(2) Although marginal forms of employment existed even before the year 2000, the Schröder reforms (2003–2005) intended to ease the transition from unemployment or inactivity to standard employment through so-called ‘*minijobs*’ and ‘*midijobs*’. Other objectives were also envisaged, for instance, the curtailment of illegal work, especially in private households.

Prior to the former reforms, full social insurance contributions became mandatory for the main form of *minijobs* at the current level of up to 450 Euro per month.<sup>18</sup> The employer, however, pays the bulk of these contributions: roughly 30 percent shared among the main insurance categories (15% goes towards the pension system, 13% to the health insurance; the rest to other items). Employees contribute 4 percent of their earnings, but they can opt out, and most of them do.<sup>19</sup> Mini-jobbers are not covered by unemployment insurance as both sides pay no contributions; they also do not acquire health insurance coverage; but most mini-jobbers are covered by derived entitlements (i.e. through the parents or working spouses in regular employment).

*Midijobs* are jobs with an income between 451 Euro and 850 Euro monthly; employers pay full social insurance contributions (‘only’ about 21%), whereas

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<sup>17</sup> Bernhard et al. (2015); Escudero (2018).

<sup>18</sup> 300 Euros in 2003. There are also time-limited minijobs with the limit of three months per year and unlimited in terms of income, but they play only a minor role (their number declined from 286,000 (2003) to 184,000 (2016)).

<sup>19</sup> For valuable details see Düll (2018), mentioning among others: “contributions paid by employers to the health insurance system help to avoid a distortive effect on competition, but are inconsistent with the insurance principle as they are not opening up own rights of workers to health insurance. The same inconsistency arises when workers are opting out of pension contributions. The employer still has to pay contributions, but workers cannot derive own pension rights from these.”

employees' contributions increase linearly until they reach the regular rate of 21 percent at 850 Euro. As a result, employers might theoretically be inclined to transform minijobs into midijobs, but the incentive for employees is low because they lose net income at the threshold of 451 Euro. In total there are only about 1.3 million midijobs.

Back to *minijobs*: As a key element of the reform, the 15-hour limit on weekly working hours has been abolished. Hence, marginal employment can be carried out *in addition* to regular employment *without becoming subject to social security contributions* for employees. This exemption can hardly be justified with respect to the principles of inclusion:

- First, it privileges insiders who already have a standard employment relationships and potentially excludes those without any job;
- Second, it also makes it harder for mini-jobbers to transit into regular jobs because insiders who might move to better-paid jobs (or strive to move!) stay put as they have the chance of an additional untaxed income;
- Third, it serves as a Trojan horse for creating jobs with low wages because workers who already have a regular income are more willing to take low-paid side-jobs;
- Fourth, people who minijob in private household services (including *Haushaltschecks*) perversely cross-subsidise well-earning households with low-earning persons or households;
- Fifth, minijobs – last but not least – lead to foregone tax revenues and social security contributions in the range of around 4 billion Euro per year, which can be regarded as the costs of subsidising minijobs.

The total number of minijobs increased from 6 million in 2003 to 7.6 million in 2016. Whereas minijobs as the only source of income has declined slightly since the year 2009 (from 5.3 to 4.9 million), minijobs as a side-job more than doubled from 1.2 to 2.7 million. Minijobs as a percentage of total jobs, however, declined due to the favourable development of regular jobs, which might be interpreted as an indicator of the limited substitution effect (minijobs substituting regular jobs), and possibly even as an indicator of the complementarity of minijobs and regular jobs – a speculation which needs further research.

The overall evaluation of marginal employment by employer representatives turns out to be positive: Minijobs are recognised as a cost-efficient and very flexible measure for dealing with peak periods and extended opening hours. In this context, competitive branches such as retail, cleaning, catering and tourism, but also private households, take advantage of this measure. In particular, small businesses appreciate the aspect of a flexible and rapid use of marginal employment at relatively low costs. Whereas these aspects already existed before

2003, the Schröder reforms abolished the limitation on weekly working hours for mini-jobbers and thus helped to strengthen internal numerical flexibility. The tripling of declared marginal employment in private households (from about 100,000 to approximately 300,000) may serve as a further indicator of the success of this strategy. Private household employers, however, are subsidised twice through the '*Household check*' procedure: they have to pay lower taxes and social security contributions, and they can deduct the expenses from their income tax duties.<sup>20</sup>

From the employees' and trade unions' point of view, however, there is great concern about minijobs offering employers the possibility to substitute regular employment and keep outsiders in a low-income and dead-end trap which also eventually leads to low social security entitlements and poverty in old age. Transition rates in standard employment are low, thus, minijobs cannot be regarded as an adequate bridge into regular employment. Midijobs, on the other hand, lead to a somewhat higher share of upward transitions, but too few people are engaged in this type of employment relationship. Furthermore, midijobs are also – like minijobs – for the most part carried out by women (75% vs. 60% for minijobs). The outcome is thus ambivalent. Marginal employment enables many mothers to combine paid and unpaid family work, but at the same time counteracts principles of inclusion (including 'gender mainstreaming') and sustainable individual security entitlements. On the positive side, however, it should also be mentioned that young (under 25) and elderly people (over 55) are overrepresented among the mini-jobbers. These 'marginal' age groups can be considered as special target groups for inclusive growth because these groups might be (in the case of education or in the event of early retirement) predominantly interested in uncomplicated additional income sources and less in additional employment or social protection.<sup>21</sup>

(3) The Schröder reforms also deregulated one important part of *temporary jobs*, i.e. temp-agency work, or the triangular form of temporary employment relationships. Prior to this reform, the *Teilzeit- und Befristungsgesetz* of 2000 (implementing the EU directive for part-time work) eased the arrangement of fixed-term work contracts. The intention was, again, to mobilise job-to-job transitions in general and the transition from unemployment to employment in particular. Fixed-term contracts altogether, however, have slightly decreased since then; they are mainly related to first jobs, in particular of young people. According to most recent figures, about 40 percent transit after the end of the contract into regular employment, 36 percent into another fixed-term contract, and

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<sup>20</sup> For further and more detailed information, again, visit the excellent study by Nicola Düll (2018) for the European Commission.

<sup>21</sup> 61 percent of mini-jobbers with main jobs are below 25 or older than 55; among the mini-jobbers in side-jobs this percentage is only 28.

25 percent become inactive or unemployed again.<sup>22</sup> The current grand coalition government intends to abolish fixed-term contracts without reason, yet it remains open whether this gets into ‘real law’ without compromises towards the many employers who disagree. In the following I turn to the more dynamic (and more interesting) element of temporary work: the triangular labour contract.

The Schröder reforms almost completely deregulated temp-agency work (or *Leiharbeit*, *Arbeitnehmerüberlassung*) only with the remaining provision that the employment relationships shall be controlled by collective agreements. Under this provision, collective agreements even allowed us to deviate from the principle of equal treatment – a form of regulation which bluntly violates the inclusion principles. Furthermore, the government at that time (under chancellor Schröder) did not expect the competition between trade union representatives in the temp-agency sector would develop into a harsh power battle between unions under the umbrella of the *Deutscher Gewerkschaftsbund* (DGB) and unions under the umbrella of *Christliche Gewerkschaften Zeitarbeit und PersonalServiceAgenturen* (CGZP). For instance, a collective agreement of the so-called Christian (sic!) Trade Union allowed *Schlecker* (a former German employer in retailing which has since gone bankrupt) to close many shops and rehire the workers through a dubious temp-agency firm which paid its workers 30 percent lower wages than before and provided much less generous fringe benefits like holidays and Christmas payments. This led to a charge against CGZP by ver.di (a large DGB trade union) which eventually succeeded because the CGZP did not fulfill the clause on representing the majority of the corresponding retail workers. In the meantime, the so-called *Tarifautonomiestärkungsgesetz* of July 2014 established a mandatory *minimum wage* (8.50 Euro in 2015, 8.84 Euro since January 2017) which solved many problems related to temp-agency work.<sup>23</sup>

Temp-agency work (officially *Leiharbeit*) has increased rapidly from a level of about 200,000 to over one million since 2015, however, with a lower speed than before. Although its share of employment reaches only 2.8 percent, 14 percent of transitions into unemployment and 19 percent of transitions from unemployment into employment come from temp-agency workers.

Nowadays, *Leiharbeit* is commonly accepted as a legitimised instrument of flexibility for employers and the overall economy. The social and even the economic risks connected with this employment relationship, however, are still not managed satisfactorily. For employees, the risk of unemployment is almost five times higher than for regular employees (3.06 vs. 0.63), but only a minority of temp-agency workers are covered by UI; most of them receive only ALG II

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<sup>22</sup> Figures reported by newspapers referring to IAB.

<sup>23</sup> For a summary of respective regulations and first insights from evaluation studies about the impacts see Bruttel et al. (2017).



(*Hartz IV*).<sup>24</sup> Furthermore, many temp-agency workers are low-wage earners; 5 percent of temp-agency workers (with 75% working full-time!) receive additional transfers of *Hartz IV*, compared to 2 percent of ‘regular’ workers. Average wages of temp-agency workers are far below those of regular workers. Approximately 50 percent of temp-agency workers are contracted out for less than three months. The envisaged stepping stone function – transitions from temp-agency work to regular work – is rather modest (at most for about 20 percent); for unemployed, however, these stepping stones are at least marginally better than for those who do not use this opportunity.<sup>25</sup>

From an inclusive point of view, however, three features of current temp-agency work in Germany are still quite problematic:

- First, even the recent reform of the *Arbeitnehmerüberlassungsgesetz* (21.02.2017) did not fully establish the equal treatment principle. Equal pay only has to be realised after nine months of continuous employment (in 2017, only 30 percent of temp-agency workers reached this level), and collective agreements can even legitimize unequal pay for up to 15 months.
- Second, although the new regulation now stipulates the maximal duration of ‘*Entleihung*’ at 18 months (the Schröder regulation set no time limit at all), practically it is still possible to recruit the same temp-agency workers permanently: a break of three months after 18 months (probably bridged by unemployment benefits) is enough to rehire the same worker. Thus, that principle of temp-agency – that it should only temporarily bridge the lack of a workforce (typically seasonal or replacing workers on parental leave) – is bluntly violated. Temp-agency work still opens the door for lower rather than regular wages and de facto discrimination against workers.
- The negative indirect economic repercussions of this regulation should not be underestimated, as with this instrument employers have a convenient instrument of flexibility. They can relax and neglect long-term investments in a larger part their staff, thus deepening the cleavage between insiders and outsiders. Furthermore, the expected overall impact on productivity, innovation and competitiveness is more than doubtful: both microeconomic and macroeconomic research hints more towards a negative impact.<sup>26</sup>

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<sup>24</sup> Bundesagentur (2018, 14).

<sup>25</sup> Lehmer/Ziegler (2010).

<sup>26</sup> See Schmid (2018b), including more references.

### 2.3 *Transitions between employment and unemployment*

The key part of the Schröder reforms were directed towards speeding the transition from unemployment to employment in general and preventing long-term unemployment in particular through the '*modernisation of labour market services*'.<sup>27</sup> Apart from the already mentioned 'Ich-AGs' (transitions from unemployment to self-employment) and the minijobs (thought of as stepping stones to regular jobs), these reforms consisted of five main elements ('*Module*')

(1) The first part of the administrative reforms can be subsumed under the strategy to *activate the unemployed* through 'supporting and demanding' ('*Fördern und Fordern*') measures. The supporting measures were mainly an improvement of placement services, especially through a larger and better-trained staff responsible for placement services and employment promotion. The demanding measures mainly consisted of tightening the rules on accepting a 'suitable' job and in reducing unemployment benefits for older people. In this context, it should be noted that prior to the Schröder reforms, older employees were eligible for wage-related benefits for up to 32 months. As a consequence of this particular legal condition, employers frequently made use of the 'golden handshake' option, thus shifting their older employees into early retirement. Such arrangements were facilitated by the pension system, which allowed retirement at the age of 60 without a corresponding actuarial reduction of pension benefits. Both rules were adjusted: the duration of unemployment benefits was cut to 12 months, or to 18 months for people aged over 55 (now, after a minor reform, up to 24 months). Furthermore, in cases of early retirement, the pension regulations now foresee an actuarial reduction of benefits. It is – at least partly – due to these new regulations that in the course of the economic upswing the employment rates of elderly employees have risen, while their unemployment rates have decreased significantly.

(2) Since the reforms, *profiling* is used to divide jobseekers into client groups (job-ready, counselling, and intensive-service clients) according to their distance from the labour market. The classification of clients serves as a basis for individual action plans and for allocating labour market services. The clients' streamlining is organised according to strict schedules in order to ensure individualised counselling and to avoid waiting queues. These measures have certainly improved the lot of the first two groups. The 'intensive-service clients', however, are even more neglected than before.

(3) *Services to employers* are improved through time-budget allocation for such services (at least 20 percent of the agencies' time) and 'premium' clients, faster reaction times, prior contacts to both employers and jobseekers, referral of a

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<sup>27</sup> See again the report of the Hartz-Commission (consisting – apart from its head Peter Hartz – of 14 people) which, unfortunately, only few people have read (if any, except the members of the commission); see Hartz (2002).

limited number of qualified contacts, follow-up contacts, an improved vacancy database and monitoring the matching process. The central goal lies in obtaining employers' attention and willingness to cooperate and, thus, increasing the share of notified vacancies. These measures have also considerably improved matching efficiency.<sup>28</sup>

(4) The reform also puts an emphasis on *privatisation* in the form of the outside provision of placement services. Most of the corresponding instruments, however, especially the Personnel Service Agencies (PSA), have not been successful.<sup>29</sup> PSAs are temporary work agencies for the unemployed that are established on a contract basis with a local service provider, which is in many cases part of the temporary work industry. This instrument, however, has failed to live up to the Hartz Commission's great expectations, mainly because the amalgamation of placement and temporary work functions have sent ambivalent signals to both the PES agencies and their clients. After a process of learning and calibration, the instrument of issuing placement vouchers to persons who had been unemployed for more than six weeks turned out to be only partially successful. Private agencies are paid a maximum of 2,000 Euro for placing an unemployed person in an employment of at least 15 hours per week: 1,000 Euro after an employment duration of at least six weeks and an additional 1,000 Euro after a duration of at least six months.

(5) The main, albeit ambivalent, impact was due to the *merging of unemployment assistance and social assistance*. Prior to the reform, the PES administered two types of benefits, which de facto defined its clientele for active measures: unemployment benefits (*Arbeitslosengeld*), which provided payments at a level of 67 percent (unemployed with children) or 60 percent (unemployed without children) of previous net wages for 12 months (or up to 32 months for older employees), and unemployment assistance (*Arbeitslosenhilfe*) after eligibility for regular unemployment benefits had expired. Unlike unemployment benefits, unemployment assistance was means-tested, amounted to 53 to 57 percent of previous net wages, and was paid for an unlimited period as long as PES could not provide a 'suitable' job. A third type of benefit was the so-called social assistance (*Sozialhilfe*), in other words, means-tested benefits at the subsistence level. Social assistance for unemployed people who were not eligible for PES benefits was funded and administered by the local authorities, the counties and the larger municipalities. On average, about 80 percent of total social assistance expenditure was funded by the local authorities, while the remaining 20 percent was funded by the German federal states (*Länder*).

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<sup>28</sup> One of these studies came to the conclusion that the organisational reforms explain about 20 percent of the decrease in unemployment, whereas the reform of unemployment benefits explains only about 5 percent, cf. Launova/Wälde (2016).

<sup>29</sup> See Hess et al. (2006).

This complex system of benefit provision had important consequences for the provision of job-brokering and other active measures for the unemployed in Germany:

- First, more and more unemployed were no longer eligible for regular unemployment benefits, rather only for means-tested unemployment assistance or social assistance.
- Second, the PES focused its active programmes de facto on its own core clientele of unemployment benefit recipients, who were being funded through the PES budget; other unemployed were either eligible for unemployment assistance administered by PES but were financed by the national government or had to apply to the local authorities for social assistance; recipients of social assistance administered by the local authorities and other unemployed persons not eligible for PES benefits were generally excluded from active PES programmes.
- Third, as a response to the unemployed who depended on social assistance, local labour market programmes for the long-term unemployed were mushrooming under the auspices of the local authorities.
- Fourth, many of these local programmes were explicitly aimed at shifting the unemployed back under the responsibility of the PES; this was possible by creating intermediary jobs lasting up to 12 months, thereby entitling the participants to regain eligibility for unemployment benefits and thereafter unlimited unemployment assistance. In the end, the losers of this shifting of responsibilities (labelled by some experts as '*organised irresponsibility*') were the long-term unemployed, especially low-skilled and older people, which was reflected in over-proportional unemployment rates in these target groups.

Under these conditions, the unlimited allowance of means-tested, yet wage-related, unemployment assistance turned out to have negative effects on work incentives, especially for those unemployed with prior earnings that had been relatively high. As this regulation also encouraged the use of 'golden handshakes', the unemployment insurance system prior to the Schröder reforms practically excluded many elderly people from participating in the labour market in exchange for generous early retirement schemes. Viewed from the regulatory idea of an inclusive labour contract – see last section – one can also put this in other terms: Both employers and (elderly) employees were released from the obligation of adjustment to structural change on the cost of the shrinking active members of the labour market who – at the end of the day – had to finance such an expensive early retirement scheme.

The Schröder reforms overhauled this highly flawed incentive system by replacing unemployment assistance with a so-called 'basic (income) security'

(*Grundsicherung*, or *Arbeitslosengeld II*). ALG II, better known as *Hartz IV*, is a means-tested and flat-rate allowance for *all* jobseekers who are not entitled to unemployment benefits, no matter whether they are clients of the local authorities (formerly social assistance recipients) or clients of the PES (formerly unemployment benefit recipients). The reform established thereby two completely separate regulatory systems (*‘Rechtskreise’*) for jobseekers: with the *Sozialgesetzbuch III* (SGB III) setting the rules for ALG I recipients and the *Sozialgesetzbuch II* (SGB II) setting the rules for Hartz IV recipients. Most importantly, from an inclusive growth perspective, is the fact that the definition of an employable jobseekers was now extended. All those who are able to work at least three hours per day are now employable and fall under the ‘regulatory circle’ of SGB II.

The impact of this part of Schröders reform – often neglected by critical opponents – was an improvement of the inclusion in the labour market in two respects:

- First, more jobseekers (unemployed) are now covered by the broader unemployment insurance (ALG I and ALG II) system: the coverage increased from 79 percent (2003) to 92 percent (2015), although the share of ALG I recipients declined from 38 to 26 percent, whereas the share of ALG II recipients increased from 41 to 66 percent.<sup>30</sup>
- Second, all ALG II recipients are now included in the system of ‘active labour market policy’, although to some extent under less favourable conditions than ALG I recipients (e.g. excluded from supported start-up measures).

The corresponding administrative reform, however, was not fully successful in establishing corresponding ‘job centres’ or one-stop shops for all of the clients under the clear responsibility of the PES, as the Hartz Commission had recommended. Due to the complex interrelationships under German federalism and a political stalemate between the leading parties, a compromise emerged which again established fragmented responsibilities between the PES and the local authorities with respect to the recipients of ‘basic security’.<sup>31</sup>

The current level of social protection for jobseekers outside the unemployment insurance system in the narrower sense (ALG I) is the following (January 2018): For a needy single unemployed person, *Hartz IV* pays an allowance of 416 Euro per month; married adults receive 90 percent (374 Euro); also – in the case of need – costs for accommodation are paid. In the case of an unemployed family

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<sup>30</sup> These figures are calculated from Table IV. D.1, Bundesagentur für Arbeit: Arbeitsmarkt 2015, p. 112.

<sup>31</sup> The majority of jobcentres at the regional level are cooperative ‘*Arbeitsgemeinschaften*’ between PES and the municipalities; a smaller part is run only by municipalities.

with two children (four and 12 years old), the family may receive altogether: 2x374 Euro + 240 Euro (child four years old) + 296 Euro (child 12 years old) + 644 Euro (accommodation and heating) = 1,928 Euro minus 388 Euro 'Kindergeld', which makes a total of 1,540 Euro.<sup>32</sup> This sum corresponds roughly to the gross wage of one full-time wage earner working at the minimum wage (8.84 Euro). Under certain circumstances, additional allowances can increase the amount of the transfer income. The transfer recipients can also earn some additional income up to a certain amount. As a result, economic incentives to work turn out to be rather mean for low-income earners, in some cases even negative. Furthermore, all 'basic security' recipients are entitled to active labour market policy – almost to the same extent as recipients of regular unemployment benefits.

Taken all together, this element of the Hartz reforms created losers as well as winners. The losers are mainly relatively well-paid former unemployment assistance recipients; the winners are former social assistance beneficiaries who are now also eligible for active labour market policy measures.

This reform did not solve, and even aggravated, at least five problems:

- First, long-term unemployed who are disadvantaged either by age, low skills or limited work capacities, still have few chances to transit to a sustainable job with a decent income. Furthermore, the PES' or the job centres' staff administering activation programmes are often not qualified enough or are overloaded; many having only fixed-term contracts. Thus, long-term unemployment is still at a level of 850,000 (34 percent of the total of 2.5 million), and a growing part of these people are unemployed for longer than four years.<sup>33</sup>
- Second, Germany is still suffering from a depressed employment rate of low-skilled people, which is reflected on the other side of the coin by high informal or even illegal ('black') work.

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<sup>32</sup> <http://www.bmas.de/DE/Themen/Arbeitsmarkt/Grundsicherung/Leistungen-zur-Sicherung-des-Lebensunterhalts/2-teaser-artikelseite-arbeitslosengeld-2-sozialgeld.html>; download 07.05.2018. A single person without child would receive 737 Euro (416+321 accommodation); a single person with a child up to four years old would receive 922 Euro (416+150 ['Mehrbedarf'] + 240 [child] + 464 [accommodation] - 194 [Kindergeld] - 154 [Unterhaltsgeld]).

<sup>33</sup> The current plan of the government to provide up to 150,000 jobs in the 'social labour market' for the long-term unemployed during the next four (sic!) years might simply not be successful because the PES does not have enough personal capacities to implement this programme. In a joint venture, trade unions' and employers' representatives of PES deplored this paradox situation in a public letter; 'paradox' since in the last years the PES' budget already made surpluses just for this reason, welcomed of course by the then finance minister Schäuble who was obsessed with the idea of a zero budget. Nevertheless, administrative costs of PES are reported to be 4.43 billion Euro, i.e. 21 percent of 21 billion expenditure for ALG II, not a sign of high efficiency..

- Third, there remains the problem of the working poor, whose earnings (often despite full-time work) fall below the minimum income and who therefore receive ‘basic security’ to top up their incomes (currently about 800,000).
- Fourth, the procedures of calculating the ‘*Grundsicherung*’ became extremely bureaucratic leading to many individual suits against the false or delayed decisions of the Hartz IV administration. The German law is obsessed with the ideal of individual case justice (*Einzelfallgerechtigkeit*), leading to bizarre excesses of bureaucracy.<sup>34</sup>
- Fifth, sanctions mechanisms against people not accepting job offers (or misbehaving in other ways) were too harsh, especially against young people under 25. Furthermore, the ‘basic allowance’ amount did not follow the real average wage income.

Altogether, this part of the Schröder reforms gained such a bad reputation that ‘Hartz IV’ – despite some crucial positive elements – became the stereotype for a ‘neoliberal’ policy that eventually broke the neck of the Social Democratic Party. Currently (May 2018) there is a hot political debate that will probably lead to a basic reform of the ‘Grundsicherung’.

#### 2.4 *Transitions between employment and unpaid (family) work*

Under the inclusive growth perspective, issues of equal opportunity for women and work-life-balance become crucial. The already mentioned *Teilzeit- und Befristungsgesetz* of 2000 made it easier to arrange part-time contracts and to ensure principles of inclusion such as equal treatment in terms of wages, dismissals and social protection. As in many other EU member states, part-time jobs increased steadily, in particular for women, and this employment dynamic is – in contrast to other forms of non-standard work – unbroken.<sup>35</sup> One of the hottest issues in the current political debate is the intention of the new government (enforced by the social democratic party) to establish an effective *right to intermediate part-time*, which means the right to take part-time work and return into full-time under equal conditions.

Even for men it has become slightly more attractive to work part-time, especially following the reform of parental leave in 2007. The new parental leave allowance (‘*Elterngeld*’) is inclusive in as far as it also covers the income risk due to transiting into full ‘inactivity’ or to intermediate part-time work due to parental

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<sup>34</sup> Just to mention one example: A married couple (‘*Bedarfsgemeinschaft*’) with one child gets divorced; she may receive Hartz IV, he is a full wage earner. When the child visits the father during the weekend and has breakfast and dinner with him, these days have to be deducted from the calculation of the child allowance for the mother. The Hartz Commission tried to avoid such awful little things through the provision of generous lump sums.

<sup>35</sup> See also Figure 3 below.

care work. In other words, income loss due to full-time or part-time leave is now insured, like in the case of ‘full-time’ unemployment, by 67 percent of the former net wage income. The condition is to some extent a kind of gender risk-sharing. Of the 14 months in which *Elterngeld* is paid, at least two months have to be taken up by men. Such a leave allowance might also be considered as an element of employment insurance although it is formally not included in UI and is not financed by individual or employer’s contributions. Moreover, the entitlements are portable from one employer to another and to any other location in the country.<sup>36</sup>

In 2015, this law was extended by another innovative element. The ‘*Elterngeld Plus*’ now supports all those parents who want to work even during the time of receiving this allowance. In this way, mothers and fathers have the possibility to extend the (pro rate) supported time of parental leave up to two years: One month *Elterngeld* doubles to two months *Elterngeld Plus*: If both parents share child care equally by working 25 to 30 hours per week, they receive four additional months, called *Partnerschaftsbonus*. The take-up of the new scheme is very encouraging. The new government allocated 6.4 billion Euro to this item in 2018.

## 2.5 Transitions between employment and (early) retirement

Transitions to early retirement only due to age reasons have been starkly reduced since the labour market reforms under Schröder. In the 1990s it was not unusual, in particular for men, to retire early aged 55 or 58 supported by generous transfers or golden handshakes (see above). Later, under the first grand coalition, the retirement age was even lifted from 65 to 67, stepwise to be implemented from cohort to cohort until 2029. The last grand coalition, however, eased again the possibility to retire at 63 for people who had completed 45 years of continuous employment covered by social security.

Nevertheless, this little reform against the overall spirit of increasing working life time produced only a small dip in the rising trend of the *average retirement age*, which increased from about 62 (2000) to 64 (2016).<sup>37</sup> The inclusive impact into the labour market is even strongly reflected in the labour force participation of people aged 56 to 65, which rocketed from 48.1 (2006) to 68.6 percent in 2016, more than 20 percentage points within 10 years!<sup>38</sup>

Transitions to early retirement due to health reasons (*Erwerbsminderung*), however, still make up 18 percent of all retirement flows (20 percent in 2000),

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<sup>36</sup> For details and evaluation see Bergemann/Riphahn (2015).

<sup>37</sup> For women it is even slightly higher than for men.

<sup>38</sup> See also Figure 4 below for the age group 58 to 67.



with an average retirement age of 52 for men and 51 for women.<sup>39</sup> The employment rate for people with restricted work capacity is only 35 percent (UK 36%); the unemployment rate in Germany is one of the highest and is above the EU28 average of 18 percent.<sup>40</sup> The number of severely disabled people who are unemployed rose by 1.2 percent from 2009 to 2016, although total unemployment declined by 21.2 percent; during the same time period, the number of participants in labour market policy measures fell by 35.4 percent!<sup>41</sup>

From the inclusive growth perspective, the labour market (policy and law) reform for the integration of severely disabled people in 2001 was in theory quite modern in anticipating some key principles of the UN Convention of 2008. The law stipulated *the right of disabled people* against their employer to

- a job that enables them to utilise and to develop further their abilities and knowledge
- privileged access to firm-specific training
- facilitation of their participation in external training
- a work environment that conforms to their disability, and
- a workplace that is equipped with the required technical facilities.<sup>42</sup>

This reform, which can be labelled a '*negotiated capacity building through accommodation*', corresponds to the general TLM strategy of extending work opportunities through 'making the market fit to workers' with the aim of greater social inclusion. This means enriching the standard employment contract by imposing on employers duties of reasonable adjustment in favour of workers, especially for those with reduced work capacity. In other words – and recently also formulated by Simon Deakin in a joint publication with Alain Supiot – rather than requiring the individual to be 'adaptable' to changing market conditions, the employment contract requires that employment practices be adapted to the circumstances of the individual.<sup>43</sup>

It is evident that these kinds of adjustment duties require support through procedural rules, for instance, negotiation through collective agreements, social pacts or covenants between firms and other key actors in the local or regional labour market. At the firm level, i.e. the case of workplace accommodation for severely disabled people, German law envisages clear procedures to be taken in order to ensure the maintenance of the employment relationship through, for

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<sup>39</sup> The dominant reason being 42.8 percent for psychic (and not, as expected, for physic) reasons, with an upward trend of this share!

<sup>40</sup> Figures from Berger (2015).

<sup>41</sup> Figures from DGB (2016); according to these figures, the activation ration for the disabled is only 18% compared to 25% of all unemployed .

<sup>42</sup> SGB (Sozialgesetzbuch) IX, §81 (4).

<sup>43</sup> Deakin (2009, p. 28), provides good practices mainly related to disability policy in Europe, an emphasis that correctly reflects the salience of this problem as also noted by Amartya Sen (2009).

example, the involvement of rehabilitation experts, ‘integration management’ and ‘integration agreements’ (§§ 83, 84 SGB IX).<sup>44</sup>

Yet, as the figures above suggest, the reality in implementing such rules is far from the ideal. Complementary regulations are necessary which – to some extent – have been considered in a new and complementary law. Therefore, the *Bundesteilhabegesetz* of 2016 stipulated or induced four important amendments:

- First, the priority of rehabilitation before pension, in other words, the priority of the right to work against the right to income replacement.
- Second, if a new job or job maintenance is ensured through workplace adjustment and/or personal assistance then the own work income (wages) is to a large extent not counted against the social transfer entitlements for disability – in other words: work pays.
- Third, works councils are now – through an amendment of the *Betriebsverfassungsgesetz* (§ 92, 3 (2)) – explicitly mandated to monitor the work priority for the disabled or people with restricted work capacities and to take initiatives for necessary adjustments measures.
- Fourth, jobcentres and pension agencies are – since the start of 2018 up to 2022 – entitled to apply for rehabilitation pilot projects for which a special budget position has been allocated (one billion Euro).

### **3. Lessons to be learned from the perspective of inclusion**

Having reviewed some theoretical foundations as well as the current policy reforms, the remainder of this paper will seek to identify a set of lessons to be derived from the German experience and under the perspective of inclusive growth. What are the major insights yielded by our analysis? Which parts of the reform can be viewed as successful? What went wrong and why? What are the strategic conclusions for re-establishing the right to work for all who want to gain self-sufficiency and individual autonomy (sovereignty) as far as possible? I start with a brief summary of the main empirical results in a stylised form (3.1), followed by a sketch of the inclusive labour contract as a regulatory idea for inclusive growth in the future digital world of work (3.2).

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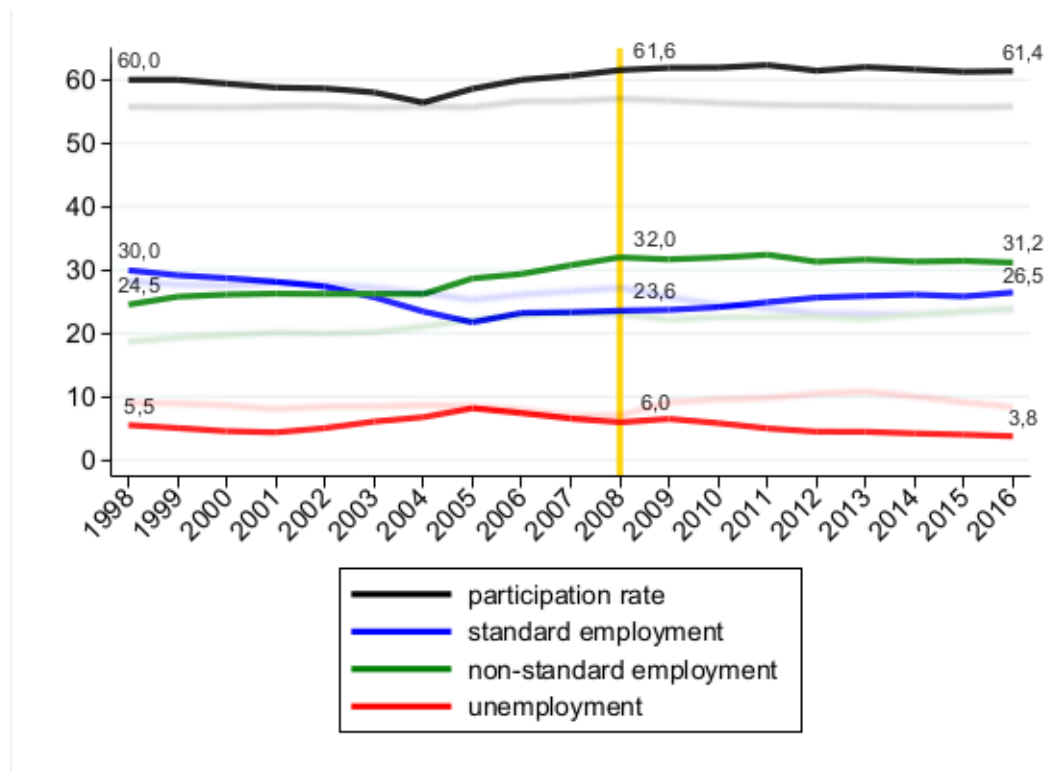
<sup>44</sup> A pathbreaking pilot project for ‘*Betriebliches Eingliederungsmanagement*’ is described in Giesert et al. (2013) which tried to institutionalise a kind of ‘employability coaching’.

### 3.1 *Stylised outcomes of German labour market reforms*

Inclusive growth has at least two dimensions: quantitative and qualitative. In quantitative terms, the main indicators of inclusive growth are employment and unemployment of the working-age population in general, and for vulnerable groups in particular (youth, elderly, women, disabled). In qualitative terms, the main indicators are working conditions, the employment relationship reflecting the degree of labour market security and social protection through work, and risk of income poverty. As I have already hinted to some detailed outcomes in describing and explaining the German labour market reforms, I confine myself in the following to rather stylised outcomes and in the order of the TLM framework.

(1) On a highly aggregated level, the German youth labour market is quite inclusive, and the degree of inclusion has even slightly improved (see black line in Figure 1): The overall participation rate for youth and young adults (15–27) increased from a level of 60 percent in 1998 to 61.4 percent; the corresponding figures for EU28 – displayed as a shadow line – are 55.8 percent for both years.

*Figure 1: Labour market participation of youth and young adults in age 15–27 in Germany as percent of population aged 15–27 (1998–2016)(shadow lines for EU28)*

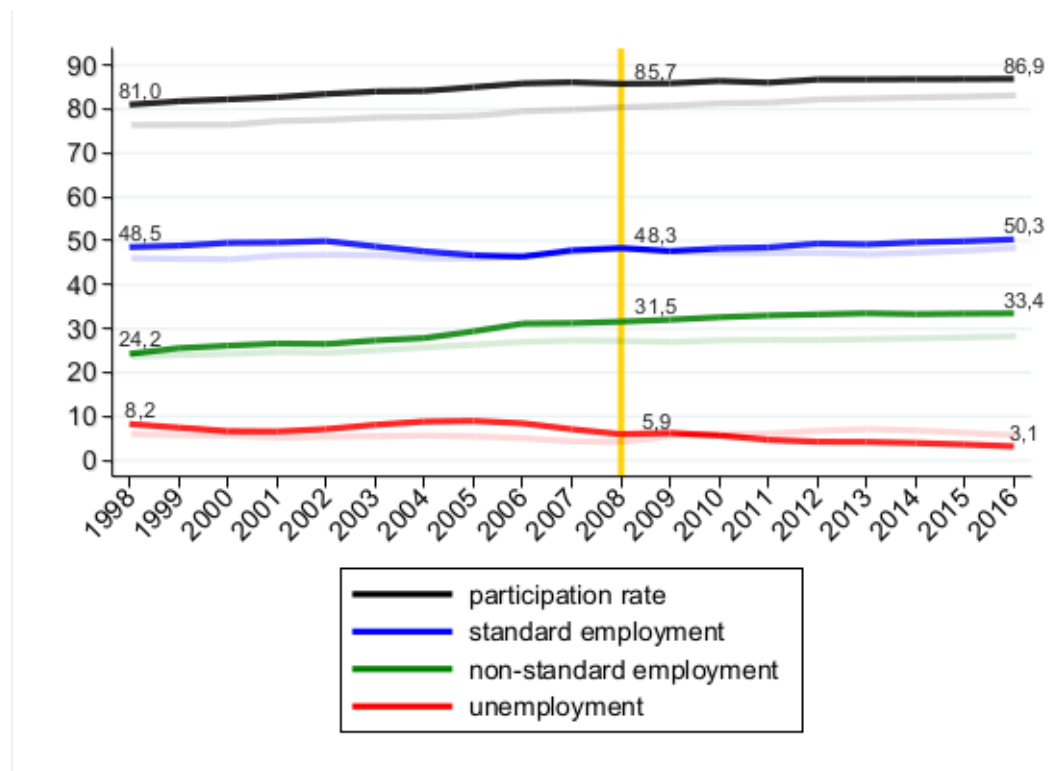


The aggregate inclusion is composed, however, by 31.2 percent employment in risky non-standard forms (see green line: part-time, temporary or self-

employment),<sup>45</sup> which increased and substituted to some extent standard employment relationships (see blue line: dependent and open-ended full-time wage work), which is now at the level of 26.5 percent, yet back on a slightly improving trend. On the other hand, the level of youth unemployment fell substantially to 3.8 percent, compared to still 8.3 percent for EU28. Note that all figures refer to the corresponding working age group; (youth) unemployment is usually measured as a percent of the corresponding ‘active’ workforce (employed plus unemployed youth) resulting in larger figures; all coloured lines, therefore, add up to the black line.

(2) The level of inclusion measured by labour market participation of the core working age group (28 to 57) also improved at the aggregate level (Figure 2): Overall, labour force participation increased from 81 percent (1998) to 86.9 percent (2016) and is substantially higher than for EU28 (see shadow line: 76.8 percent and 83.5 percent).

*Figure 2: Labour market participation of the LM core group in age 28 to 57 in Germany as percent of population aged 28 to 57 (1998–2016)(shadow lines for EU28)*



<sup>45</sup> Controlled for overlapping; see for definitions and details (which also holds for the following figures) Schmid (2018b) and Schmid/Wagner (2018).

Only a minor part of this growth, however, was due to there being more people in regular jobs at a level corresponding to the EU28 average; most of this growth is related to the increase of non-standard labour force participation (green line) from 24.2 to 33.4 percent. The comparative lines show that the rising gap between Germany and EU28 started with the Schröder reforms. On the other hand, unemployment (red line) started to go down at about the same time by 5.1 percentage points from 8.2 to 3.1 percent whereas unemployment for this age group at the EU28 level remained almost constant (6.4 vs. 6.1 percent).

(3) Regarding the transition between employment and unemployment or vice versa, transition probabilities would be the proper information to reflect the changing dynamics induced through labour market policy or labour law reforms. As stylised outcome, however, one single and crude indicator should suffice for this aim: the dynamic and changing relationship between short-term and long-term unemployment. As long-term unemployment is the real evil to fight because being out of work for a long time excludes individuals from participation not only in gainful employment (with increasing poverty risks) but also (indirectly) from participation in social and political realms, keeping long-term unemployment as low as possible is of utmost importance for social inclusion.

*Figure 3: Total unemployment rate, broken down in its components of short-term and long-term unemployment, as a percentage of the working age population in age 15 to 67 in Germany (2002–2017)(shadow lines for EU28)*

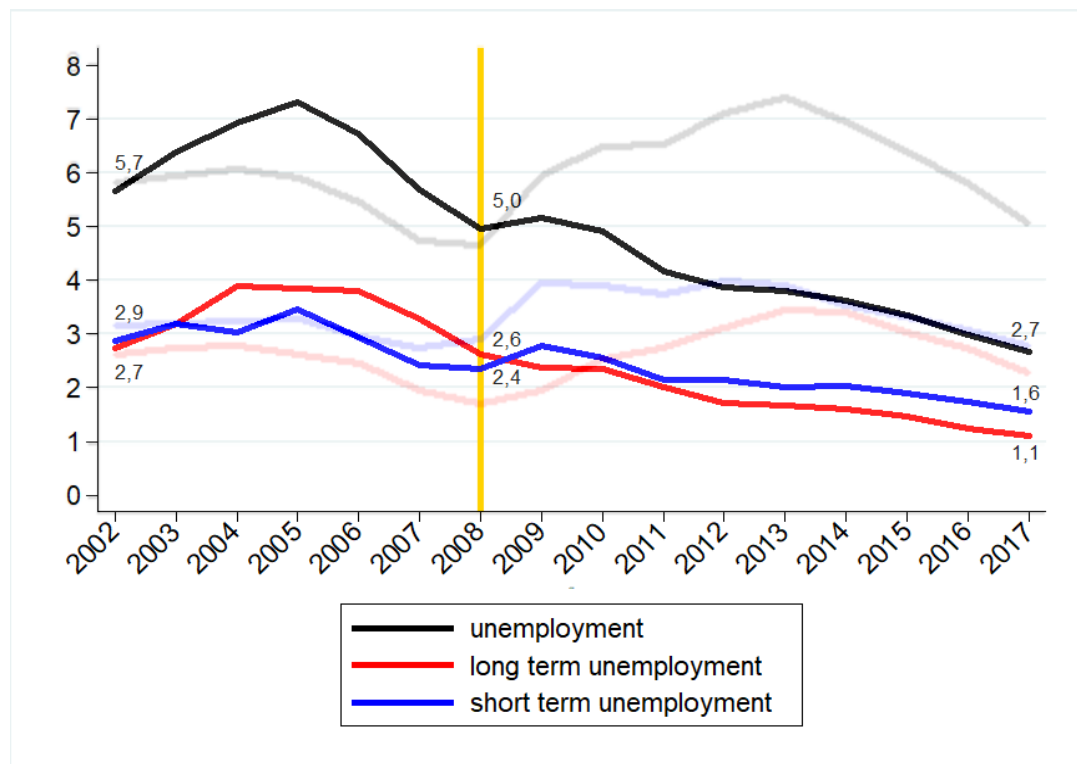


Figure 3 shows therefore the development of total unemployment as a percentage of the population in working age 15 to 67 in Germany from 2002 to 2017 (with EU28 as shadow lines), broken down into two components: the short-term unemployment rate (unemployed with a duration up to one year), and the long-term unemployment rate (unemployed with a duration longer than one year).<sup>46</sup>

The curves of Figure 3 reveal some interesting facts: First of all, compared to the total EU28 community, German unemployment jumped during the first years of the Schröder reforms to a historical high: 4.5 million unemployed on average in year 2005. Or to put it more drastically: Of the 21 million unemployed in Europe, almost every fourth or fifth was German; Germany was the “sick man of Europe.” Then, however, the reforms quickly became effective and the level of total unemployment decreased more rapidly than in EU28. Second, in sharp contrast to EU28, total unemployment remained almost constant during the recession in 2008/09, in particular due to internal flexibility measures. Third, the resilience of the ‘German model’ proved its strength during the aftermath of the recession: total unemployment went further down whereas most of the other EU memberstates experienced a further increase up to a level of 26.3 million in 2013. Since then, fourth, the German unemployment dynamics ran parallel to EU28.

The relationship between short-term and long-term unemployment also improved considerably. In EU28 as an aggregate, the share of long-term unemployment never exceeded short-term unemployment; both curves came near together only in 2013/14. As the Schröder reforms were initiated, however, long-term unemployment started to exceed short-term unemployment: In 2006/07, the number of long-term unemployed was over half a million higher than the number of short-term unemployed. The situation, however, changed during and after the recession when long-term unemployment declined faster than short-term unemployment. Yet, as we already noted in the respective policy analysis above, the long-term unemployment curve is still near the short-term unemployment line, and for at least around 700.000 long-term unemployed, the risk of social exclusion is still real and high. The hard-core, i.e. those who are longer than four years unemployed, even increased or remained almost constant during the last years.

(4) Female labour force participation reflects to a large extent the transition dynamics between gainful and unpaid family work. Figure 4 shows (indirectly) that the inclusive impact of the last labour market reforms in Germany was much stronger for women than for men; it was also higher compared to EU28.

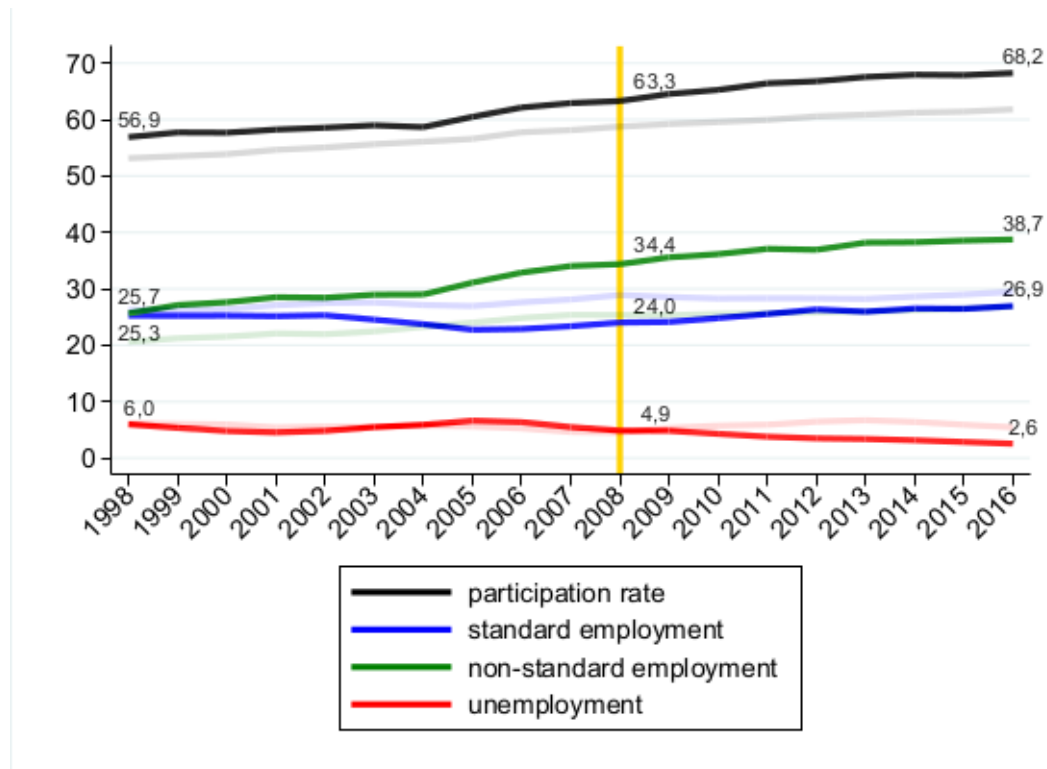
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<sup>46</sup> Note again the difference in the definition compared to the usual denominator of published unemployment rates that have the active labour force (employed plus unemployed) as denominator. Data in Figure 3 are compiled from various Employment and Social Development Reports of the European Commission and own calculations. Due to standardisation, they are not strictly comparable to the data used in the other figures or mentioned in the text.

First, unemployment improved and is below the level of men (2.6 percent women vs. 3.4 percent men). Female labour force participation rocketed within the 18-year period from 56.9 to 68.2 percent, whereas the labour force participation rate of men (not shown here) only slightly improved from 73.2 to 77.1 percent; the gender gap thereby diminished from 21.3 to 8.9 percentage points! The corresponding gender gap at the EU28 level also improved but is still at 11.5 percent.

Most of this inclusion or gender gap reduction, however, was obtained through non-standard work, in particular part-time work (green line) which is now far beyond the level of EU28 (38.7 versus 26.9 percent). With respect to regular work, German women are now even below the EU28 level (26.9 percent versus 29.5 percent); correspondingly, the German gender gap between men and women related to standard employment only slightly improved from 23.9 to 23.5 percentage points!!

*Figure 4: Labour market participation of women in Germany as percent of female population aged 15 to 67 (1998–2016)(shadow lines for EU28)*

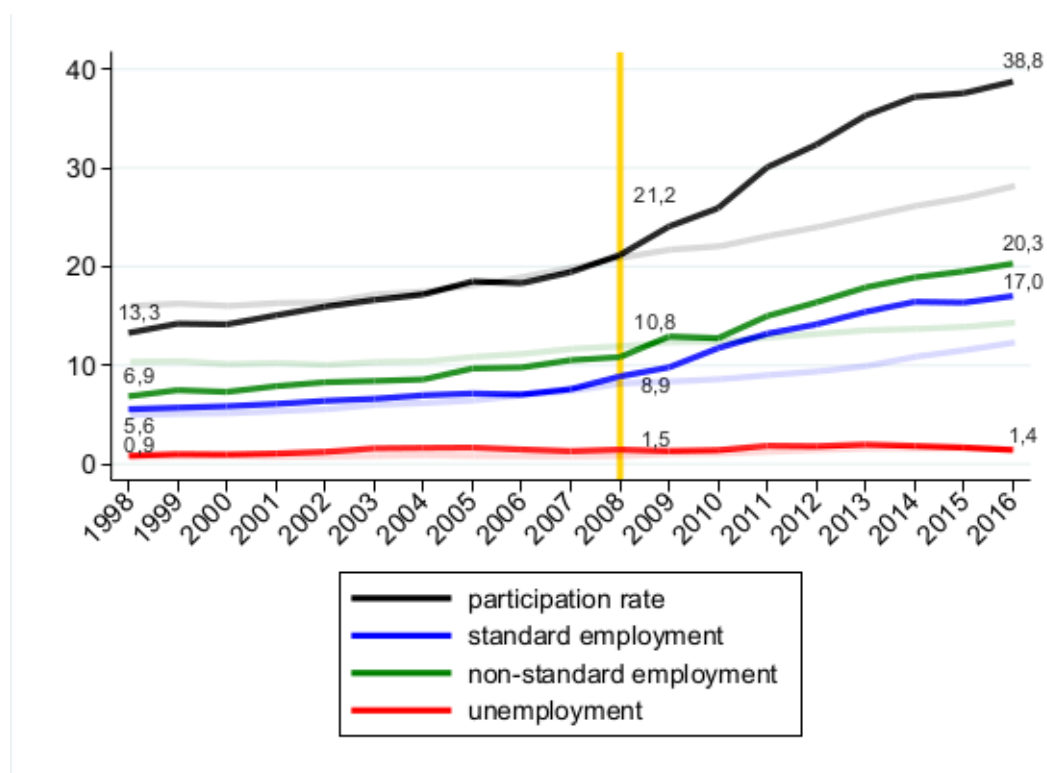


(5) Most impressive was the inclusion impact for mature aged people in the age group 58 to 67. Figure 5 tells the story. Labour force participation of this age group jumped from 13.3 percent to 38.8 percent, accompanied by a slight increase in unemployment, which reflects the stronger labour market attachment of this

group compared to the late 1990s. This dynamic was less impressive at the EU28 level where labour force participation of mature aged people ‘only’ increased from 16 percent to 28.2 percent (shadow line).

It is remarkable that this positive dynamic was accompanied by a parallel increase of both standard and non-standard employment. Finally, it is also worthwhile mentioning that the inclusion of mature aged people speeded up after the economic recession in 2008/09. Parallel improvement also happened for the EU28 average, however, not with such a stark speeding up after the recession. The non-standard participation rate for Germany in this age group is now at 20.3 percent (EU28: 14.3%), and the standard employment rate at the level of 17 percent (EU28: 12.3%).

*Figure 5: Labour market participation of elderly people in age 58 to 67 in Germany as percent of population aged 58 to 67 (1998–2016)(shadow lines for EU28)*



To sum up: Germany’s quantitative inclusive growth in terms of labour force participation was stronger than at the overall EU28 level. What about the performance in qualitative terms? As Germany’s inclusive growth was promoted to a large extent by non-standard employment, it seems plausible that the outlook at the qualitative level will turn out to be less favourable. The following Table 2 confirms this expectation.



Table 2: Indicators of qualitative inclusion in Europe, 2005, 2010, 2015

Indicator	Country	2005	2010	2015	Difference (2015–2005)
Income Poverty (percent of population <60% median)*	EU19	15.5	16.3	17.2	1.7
	EU28	16.4	16.5	17.3	0.9
	Germany	12.2	15.6	16.7	4.5
	Greece	19.6	20.1	21.4	2.8
Material Poverty (percent of population with severe material deprivation)*	EU19	6.3	6.1	6.9	0.6
	EU28	10.7	8.4	8.1	- 2.6
	Germany	4.6	4.5	4.4	- 0.2
	Greece	12.8	11.6	22.2	9.6
Earnings Capacity Poverty (as percent of population in households with low employment intensity)*	EU19	9.8	10.4	11.2	1.4
	EU28	10.3	10.,3	10.6	0.3
	Germany	12.0	11.,2	9.8	- 2.2
	Greece	7.6	7.6	16.8	9.2
Income Inequality (proportion S80/S20)	EU19	4.7	4.9	5.2	0.,5
	EU28	5.0	4.9	5.2	0.2
	Germany	3.8	4.5	4.8	1.0
	Greece	5.8	5.6	6.5	0.7

Source: European Commission, *Employment and Social Developments 2017*; Tables in Appendix, difference in percentage points.

\*) These are the three dimensions chosen by the European Commission as a weighted benchmark for being at risk of poverty or exclusion (AROPE); for definitions see:

[http://ec.europa.eu/eurostat/statistics-explained/index.php/People\\_at\\_risk\\_of\\_poverty\\_or\\_social\\_exclusion](http://ec.europa.eu/eurostat/statistics-explained/index.php/People_at_risk_of_poverty_or_social_exclusion) (download: 02.04.2018).

Apart from Greece, which was chosen as a contrasting ‘poor’ country, ‘rich’ Germany performs worse than the EU28 or EU19 (Eurozone) at three points among the selected four indicators of qualitative inclusion:

- The risk of income poverty increased faster than in the EU28 or EU19 by 4.5 percentage points from 2005 to 2015, albeit from a level below the EU average, even more so than in Greece.
- Material deprivation stagnated more or less (-0.2), albeit at a low level (‘rich’ country), whereas it declined substantially in EU28; albeit not in Greece where it extended – not surprisingly – to a broader population from 12.8 to 22.2 percent.
- The increase in income inequality in Germany was one of the highest among EU member states, again from a lower level than the European average but even more than in Greece.

The only exception among the selected indicators is earnings capacity poverty measured as the percent of the population living in households with low

employment intensity. Measured by this indicator German performance improved, which is probably a reflection of the strong quantitative inclusion impact of German employment policy.

So, is there an unavoidable tradeoff between quantitative and qualitative inclusion? The task of the final section develops the idea of an inclusive labour contract which could be the solution to overcome the tradeoff and to develop a virtuous (instead of a vicious circle) between quantitative and qualitative inclusion.

### 3.2 *The inclusive labour contract as regulatory idea*

The main message of the previous sections and developed in more details in a forthcoming book<sup>47</sup> is that we should embrace non-standard employment (NSE) as an opportunity rather than as a danger. The consequence of this view, however, is a responsibility of policymakers to ensure there are new institutional capacities that provide social protection for people engaging in these risky employment relationships, increasing in particular in terms of working time flexibility over the life course, statistically reflected imperfectly in the rising phenomenon of part-time work.

So far, the dangerous elements of risks related to NSE have been emphasised: precarious and dead-end jobs, rising inequality and segmentation. This view is certainly justified by the facts, but I hope to have added and justified a more optimistic view by pointing to the opportunity elements of risks related to NSE, that is, enhancing productivity through increasing the variability of employment relationships and greater sovereignty of workers for choosing the most suitable form of employment relationship over the life course with changing needs and preferences. The provocative news from the empirical part of the underlying study to this essay is the observation that it is voluntary part-time in particular (taken as an indicator of working-time flexibility over the life course) which seems to be an important driver for a new ‘marriage’ of equity and efficiency in the digital economy.<sup>48</sup> Furthermore, Europe should not dismiss the labour market complexity of the global world around its small continent which is, to a large extent, still strongly characterised by informal employment relationships with low social protection.<sup>49</sup>

Embracing more contractual complexity requires enhanced institutional capacities to respond to the new challenges of fair risk-sharing at three levels: the legal, the financial and the organisational level. At the legal level, a new labour standard based on the idea of an effective right to decent work (RDW) beyond formal

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<sup>47</sup> Schmid (2018a), Schmid (2018b), Schmid/Wagner (2017, 2018).

<sup>48</sup> See in particular tables 9 and 10 in Schmid (2018b).

<sup>49</sup> See also ILO (2016) and Schmid (2018a).

employment might be the solution. At the financial level, social protection – in a digital economy – may rely less on wage-based contributions and more on general taxation (including capital gains, wealth and luxurious consumption). At the organisational level, negotiated flexicurity and effective labour market services are at the core, like smart-matching demand and supply, monitoring and evaluation, case management based on individualized assessment, continuous training and vocational education, co-financing implemented within modern governance structures such as co-determination and participation in investment decisions. Germany, as shown above, provides some good practices in this respect.

As far as the legal level is concerned, expanding the range of the labour contract to all forms of work, also including unpaid but socially highly valued work as proposed, for instance, by the Supiot Report,<sup>50</sup> seems to be the most radical and promising route for ensuring social protection to workers. The main aim is the move from protecting jobs to protecting the employability of people, or from job security to labour market security.<sup>51</sup> Social security linked to traditional employment relationships would be extended in the new standard to include income and employment risks related to transitions between various employment and labour market statuses. The legal core is the establishment of new social rights and new social obligations on both sides of the labour market.

The coverage of the social rights would be new in that they would include subjects that are unfamiliar to industrial wage-earners on which the traditional standard employment relationship is built: the right to regular employability assessment, to appropriate working hours including the right to request shorter working hours, to a family life, to occupational redeployment, retraining or vocational rehabilitation. Furthermore, a flexible job guarantee through the state would be an accompanying element.<sup>52</sup> In contrast to earlier job guarantees, this guarantee would be flexible in three respects: First, individuals would be free to choose a job offer by the state. Second, individuals could combine this right with various ‘non-standard’ forms of employment, e.g. involuntary part-time. Third, the guarantee could also take the form of subsidised employment in the (private) market sector. This right is also an immediate conclusion from the insight that employment has not only instrumental but also intrinsic features, including also – as emphasised against the idea of UBI – the challenge to take personal risks. Providing job opportunities can, for instance, take youth out of their ‘natural’ neighbourhood and eliminate, at least for a certain time, the often negative effects of peer groups in disadvantaged environments.

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<sup>50</sup> Supiot (2011/2016).

<sup>51</sup> See also, among others, Auer/Gazier (2006).

<sup>52</sup> Atkinson (2015), pp. 140–7.

The scope of social rights would also be new since they would include not only 'standard' wage-earners but also the 'non-standard' part-time workers, the self-employed or semi-self-employed, the temp-agency workers, the marginal workers, and even zero-hour contract workers. One example would be including the risk of reduced earnings capacity in a way analogue to short-time work (of full-time workers) covered by unemployment insurance. The income loss induced by reduced working time (due to, for example, care obligations) could be compensated by part-time unemployment benefits or – as in the German case – a wage-related parental leave allowance. Such a benefit would also be helpful when related to the increasing demand of care for the frail and elderly which, for example in Germany, in its majority (three-fourths) is still provided within the family and again predominantly by women.

The nature of social rights would be new because they often take the form of vouchers, social drawing rights or personnel accounts, which provide transition securities from one labour contract to another and allow workers to rely on solidarity within defined and perhaps collectively bargained limits when exercising their new freedom to act.

A good practice example of such coordinated flexibility is the German collective agreement established in the chemical industry in April 2008, setting up so-called demography funds. This overall framework agreement required all employers to contribute an annual sum of 300 Euro for each employee into a fund, which could be utilised after corresponding negotiations and deliberations at the firm level for various aims, among others for training or retraining, for buying occupational disability insurance or for early retirement, however, under the condition of building a bridge for young workers entering employment. In 2015, instead of bargaining for an aggressive wage increase, trade unions successfully fought for a stepwise increase of employers' contributions into this fund: 550 Euro in 2016 and 750 Euro in 2017, corresponding to an otherwise 0.9 percent wage increase.

To the extent that these new rights enhance the range of individual choices, a corresponding new field of individual responsibilities opens up. This dimension, strangely enough, is not covered in the Supiot Report. Amartya Sen, however, is quite outspoken in this respect: "Freedom to choose gives us the opportunity to decide what we should do, but with the opportunity comes the responsibility for what we do – to the extent that they are chosen actions. Since a capability is the power to do something, the accountability that emanates from that ability – that power – is a part of the capability perspective, and this can make room for demands of duty – what can be broadly called deontological demands."<sup>53</sup>

The coverage of social obligations arising from the extended room of individual freedom to act would be new in that they would include subjects unfamiliar in the

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<sup>53</sup> Sen (2009, p. 19).

traditional employment relationship: obligations to train and retrain both for employees as well as for employers to maintain employability; to actively search for a new job or accept a less well paid job under fair compensating rules; to healthy lifestyles and occupational rehabilitation; to reasonable workplace adjustments according to the capabilities of workers or to changing working times according to the needs either related to the individual life course or to volatile market demands of goods and services. A good example in this direction are the reforms of the German law for severely disabled people, which have been described above. It is evident that these kinds of adjustment duties require support through collective agreements or social pacts between firms and other key actors in the local or regional labour market with the support of modern labour market services, which are still underdeveloped in Germany.

The scope of social obligations would also be new since they would include not only certain categories of workers or employers but also the core workers in open-ended contracts and all firms regardless of size and function. The exemption of civil servants or the self-employed from contributing to social security (especially pensions and unemployment insurance) as, for instance, in Germany, would not be justified under the regulatory idea of an inclusive labour contract. A good practice example is the obligation to work-share in the event of cyclical troughs of demand if workers' representatives (Betriebsrat) require this from the employer whereby, in turn, the law entitles them to ask employers to work-share as an instrument to maintain the employment relationship. The German scheme of short-time work (Kurzarbeit) demonstrates the usefulness of such a device for internal flexibility as well as the need to fine-tune the contractual arrangements.<sup>54</sup>

The nature of social obligations would be new because they often take the form of 'voice', involving negotiations at individual, firm, regional and branch level in order to reach mutual agreements and to accept compromises in case of different interests, so-called negotiated flexicurity.<sup>55</sup> As many workers in NSFE have a limited voice, it is important to include measures that can strengthen their ability to be heard and to negotiate effectively. Voice as an adjustment mechanism to structural change involving high uncertainty is known in the literature on industrial relations as legally acknowledged *learning communities*. Covenants are a good practice case, which – for instance – are widely used as a governance instrument in the Netherlands. A covenant is an undersigned written agreement, or a system of agreements, between two or more parties, at least one that is or represents a public authority, meant to effectuate governmental policy. There is no single format of a covenant, but they share common features: enough overlapping interests of participants, mechanisms bringing about both definition and the machinery of achievements. The parties cooperate and formal sanctions are absent, yet parties have the opportunity to go to court should one party default.

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<sup>54</sup> See for instance Möller (2010), Schmid (2015: 84–6); Storrie (2012).

<sup>55</sup> Schmid (2008:317–22).

Covenants could also be understood as a “pressure” or “incentive” mechanism for coordination to economise on the most scarce and strategic resource, that is, the ability to take adequate decisions and to avoid the decision traps of collective good production in uncertain environments.<sup>56</sup>

To sum up: The challenge of NSE could be taken as a chance to design a roadmap guided by the regulatory idea of an inclusive labour contract. New social rights and obligations under this systemic reorientation would increase the internal flexibility of ‘standard’ employment as a functional equivalent to external flexibility which often ends up in a precarious NSE. But they would also include voluntary forms of NSE in a broader social protection framework as currently exists, for instance, by extending the conventional unemployment insurance to a system of employment insurance which also covers income risks other than unemployment, such as voluntary or involuntary part-time or short-time work.

The establishment of new social rights and new social obligations according to the regulatory idea of an inclusive labour contract would also ensure the development of institutional capabilities that not only make workers fit to the market, but that also make the market fit to the workers.<sup>57</sup> The employment strategy of inclusive growth should be based on the regulatory idea of a new labour standard which goes beyond employment and includes all kinds of work that are socially valued or even obligatory. The inclusive labour contract brings together the supply strategy of investments in human capabilities over the whole life course, and the demand strategy of inclusive growth through job creation by proper fiscal and monetary policies enhanced by the protected variability of labour contracts. This would also be an essential element of a global social policy<sup>58</sup> that aims at the prevention of a vicious cycle or cut-throat global competition, originally described by the socialist political activist, Ferdinand Lassalle, as the iron law of falling real net wages towards an existence minimum.<sup>59</sup>

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<sup>56</sup> Frank (2012), Korver/Schmid (2012: 39–41).

<sup>57</sup> Gazier (2003), Schmid (2008, 2018b).

<sup>58</sup> See the interesting contributions to this topic in Deeming/Smith (2018).

<sup>59</sup> Supiot (2016, XXXVIII).

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